PES
Partners for Economic Solutions

Memorandum

To: Department of Planning & Zoning
Office of Housing

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Subject: Financial Summary of RMF Zoning Analysis

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Background

RMF zoning is a zoning category that was established to create incentives for affordable housing and allows a Floor Area Ratio (FAR) up to 3.0. The RMF zone is subject to a community engagement process and review by the Planning Commission and approval by City Council. The approval process is intended to review and mitigate potential impacts as part of the community process and approval by City Council. In exchange for this greater floor area, the approval requires a commitment to long-term affordability of one-third of the units made possible by the increase in density above the base floor area. The affordability requirement targets households with incomes averaging 40 percent of the Area Median Income (AMI). To date, five projects have utilized the RMF Zone, enabling the retention of over 350 units and the creation of over 700 net new units through redevelopment.

The RMF zones are also eligible to apply to utilize Section 7-700, the City's optional bonus density and height tool that allows an additional 30-percent increase in residential density in exchange for one-third of the incremental new units being committed as affordable units. The bonus height provision is typically used in zones that allow heights in excess of 50 feet because the greater density often requires taller buildings to fit the full building program on the site considering setbacks and other design guidelines.

Findings of Our Analysis

Given the high cost of creating and retaining units affordable to households with incomes averaging 40 percent of AMI, such projects will have a significant financial gap between their development costs and the amount of financing they can secure based on their project's revenue (rents). Due to this gap, these projects are unlikely to happen without some form of the financial assistance, such as Low-Income Housing Tax Credits (LIHTC) or other funding sources, including federal rental subsidies.

The Low Income Housing Tax Credits (LIHTC) Program

LIHTC funding is the Federal government's most important tool for supporting affordable rental housing. The program offers two levels of subsidy – nine-percent tax credits that are limited in availability and awarded competitively statewide, and four-percent credits that are available automatically for any project that uses multi-family revenue bonds. The revenue bond program serves multi-family developments that include at least 20 percent of units at rents affordable to households up to 50 percent of AMI or at least 40 percent of units affordable up to 60 percent of AMI. Our models tested both types of credits but assumed four-percent credits for mixed-income housing developed with a limited component of affordable units by a for-profit developer.

Other Funding Sources

The Housing Choice Voucher program (Section 8) allows a portion of the City's rent subsidy vouchers to be attached to specific properties rather than to individual households to deeply subsidize units. The unit may be rented at a level affordable to a household at 60 percent of AMI; the voucher pays the difference between that rent and the rent affordable to the tenant, typically at or below 30 percent of AMI. The HOME Investment Partnership Program funds can be used to support new housing development, but typically provide a small fraction of the total costs. Philanthropic and private funds, such as the Amazon Housing Equity Fund, support new construction and/or rehabilitation of affordable or workforce housing. Smaller grant programs may help to offset the cost of energy efficiency or other resiliency features. The U.S. Department of Housing and Urban Development's (HUD) Section 202 and Section 811 programs provide funding for housing for seniors and persons with disabilities. The Federal Home Loan Bank Board offers housing development grants.

Virginia Housing offers different financing programs to support affordable and mixed-income housing development. The Virginia Department of Housing and Community Development (DHCD) provides funding for affordable and special needs housing.

The City's Office of Housing works with a range of non-profit partners to fund construction and rehabilitation of affordable housing, typically in tandem with LIHTC funding.

Scenarios

PES analyzed development scenarios to test the impact of different submarkets and rent levels within Alexandria. It is noted that the multi-family development industry is facing significant difficulties with very high construction costs exacerbated by the supply chain failures during the Covid-19 pandemic and rising interest rates. After an extended period of interest rates near 3.0 percent, Federal Reserve actions to fight inflation by tightening the money supply and raising interest rates have now pushed multi-family mortgage rates to 6.7 percent and above. For much of the industry, the combination of high costs and high interest rates has undermined the feasibility of new multi-family development at the current time.

For all of the scenarios evaluated for this analysis, none of them were able to finance the construction of units without a significant subsidy.

Because all of the scenarios that we evaluated required a significant subsidy, we also evaluated a sensitivity analysis to consider other levels of affordability. For example, in addition to the RMF requirement that one-third of incremental new units be affordable to households at 40 percent of AMI, PES tested options at 50 percent of AMI and a split between 40 and 50 percent of AMI. Also tested were provisions that would require a smaller proportion of the units to be affordable, including one-fourth and one-fifth of incremental units.

The cases with smaller allocations of affordable units below 20 percent of total units showed higher subsidy requirements, because LIHTC and other subsidies are available only to developments with at least 20 percent of the units affordable at 50 percent of AMI. The loss of that LIHTC funding was a worse financial impact than the cost savings of providing fewer affordable units.

Testing an all-affordable development that was eligible for nine-percent LIHTC credits showed that the RMF provision could make the project feasible with more reasonable levels of financial support from the City, State or Federal government. For example, the nine-percent LIHTC credits covered 62 percent of the total costs for a development with all the units affordable at an average of 50 percent of AMI.

The Bottom Line

The RMF Zone has demonstrated to be an effective tool for the preservation and creation of deeply affordable rental housing; however, it will likely require a combination of tax credits, City, State and/or Federal subsidies or other tools to make future projects financially feasible. While it is not anticipated that the RMF Zone will be widely utilized throughout the city because of the financial challenges outlined above, it is an important zoning incentive that can be used in strategic locations when paired with financial subsidies and/or other tools.